BEFORE THE ARIZONA CORPORATIO

COMMISSIONERS
KRISTIN K. MAYES - CHAIRMAN
GARY PIERCE
PAUL NEWMAN
SANDRA D. KENNEDY
BOB STUMP

IN THE MATTER OF THE REVIEW AND POSSIBLE REVISION OF ARIZONA UNIVERSAL SERVICE FUND RULES, ARTICLE 12 OF THE ARIZONA ADMINISTRATIVE CODE.	Docket No. RT-00000H-97-0137
IN THE MATTER OF THE INVESTIGATION OF THE COST OF TELECOMMUNICATIONS ACCESS	Docket No. T-00000D-00-0672

NOTICE OF FILING

Eschelon Telecom of Arizona, Inc., Mountain Telecommunications, Inc., Electric Lightwave, LLC and McLeod USA Telecommunications Services, Inc. dba PAETEC Business Services hereby give notice that they are filing the attached public version of the Reply Testimony of Doug Denney on behalf of Eschelon Telecom of Arizona, Inc., Mountain Telecommunications, Inc., Electric Lightwave, LLC, McLeod USA Telecommunications Services, Inc. dba PAETEC Business Services, tw telecom of arizona, llc and XO Communications Services, Inc. ("Joint CLECS").

RESPECTFULLY SUBMITTED this 5th day of February 2010.

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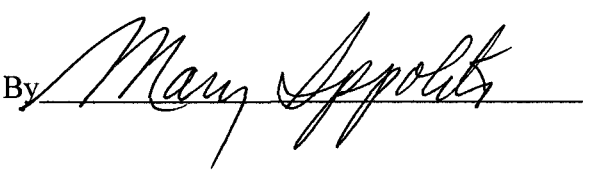
By 

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REPLY TESTIMONY

OF

DOUGLAS DENNEY

ON BEHALF OF

Eschelon Telecom of Arizona, Inc.; Mountain Telecommunications, Inc.; Electric Lightwave, LLC; McLeodUSA Telecommunications Services, Inc. d/b/a PAETEC Business Services; tw telecom of arizona llc; and XO Communications Services, Inc.

PUBLIC VERSION

February 5, 2010

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I. INTRODUCTION

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is Douglas Denney. I work at 1201 NE Lloyd Boulevard, Suite 500, Portland, Oregon.

Q. ARE YOU THE SAME DOUGLAS DENNEY WHO PREVIOUSLY FILED TESTIMONY IN THIS PROCEEDING?

A. Yes, I filed direct testimony on December 1, 2009.

Q. DO YOU HAVE ANY CORRECTIONS TO YOUR DIRECT TESTIMONY?

A. Yes. When comparing competitive local exchange carrier ("CLEC") access rates to Qwest's access rates in 1999, I omitted one of Qwest's rate elements (interconnection charge of $0.006/minute), meaning that the last row in Table 1 on p. 19 of my direct testimony, which contains Qwest's composite access rates labeled "Qwest Pre-Price Cap," should be revised upwards: The originating rate should be $0.03424 (instead of $0.02803), and the terminating rate should $0.04844 (instead of $0.04223). This correction does not affect other numbers in this table. A corrected Table 1 is presented below.

Table 1: Corrected

Table 1: Originating and Terminating Access Rate Comparison

LEC	Originating	Terminating	Source Intrastate Tariff
AT&T LEC	$ 0.02803	$ 0.04223	AT&T Communications of the Mountain States Access Services and Network Interconnection Services Price List
Verizon LEC	$ 0.05027	$ 0.07115	MCImetro Access Transmission, Tariff No. 2
Average AT&T and VZ	**$ 0.03915**	**$ 0.05669**	
Integra:			
ELI	$ 0.02990	$ 0.04270	Switched Exchange Access Telecom Services Tariff No. 3
Eschelon	$ 0.02967	$ 0.05241	Access Service Tariff No. 2
Mountain	$ 0.02967	$ 0.05241	Telecommunications Tariff No. 1
McLeodUSA	$ 0.05523	$ 0.05523	Intrastate Access Tariff No. 4
tw telecom	$ 0.03610	$ 0.04409	Intrastate Telecommunications Access Services Tariff No. 4
XO	$ 0.03434	$ 0.04854	Access Service Tariff No. 7
Average JCLECs	**$ 0.03582**	**$ 0.04923**	
Qwest Pre-Price Cap	**$ 0.03424**	**$ 0.04844**	See note below

Current tariffs can be found on the ACC website: http://www.azcc.gov/Divisions/Utilities/Tariff/util-tarrifs-telecom.asp. Qwest's historical access rates are based on Docket No. T-01051B-99-0105 (1999 Price Cap Docket), Testimony of Barbara M. Wilcox on behalf of Qwest, January 8, 1999, Exhibit BMG-5.

Q. WHAT IS THE PURPOSE OF THIS TESTIMONY?

A. The purpose of this testimony is to respond to selected issues raised in direct testimonies of other parties as they relate to the issues and positions of the Joint

CLECs as outlined in my direct testimony. Like my direct testimony, this testimony is organized by issue as they were outlined in the procedural order.[1]

Q. PLEASE SUMMARIZE YOUR TESTIMONY.

A. No party has demonstrated that Joint CLEC access rates are unjust or/and unreasonable or above cost. The mere desire by interexchange carriers ("IXCs") to avoid paying to use local exchange carrier ("LEC") networks is not justification to reduce intrastate access rates in Arizona. Parties that point to interstate access rates as the alleged evidence that intrastate rates should be reduced do not make an "apples-to-apples" comparison because that fails to account for the difference in the *structure* of the two rate schemes: (interstate switched access charges include the federal Subscriber Line Charge ("SLC"), a rate element not instituted by the state of Arizona. Staff's witness, Mr. Shand, recognizes this difference. When SLC is factored in, the federal composite interstate access rate (rate applied to Qwest and CLECs) is approximately 3.57 cents per minute, which is higher than Qwest's intrastate access rate in Arizona.[2]

Further, the issue of whether rates of specific carriers/groups of carriers are "unreasonable" or/and "below cost" should be considered separately from the issue of "from whom should the cost be recovered" (end-users or IXCs). Because IXCs use networks of local exchange carriers to the benefit of IXCs and IXC end-

1 *Procedural Order*, September 29, 2009, pp. 4-5.

2 This is discussed in detail with respect to, "Issue 2. To what target level should access rates be reduced?"

users, it is unfair to shift the burden of the network cost to LECs and LEC end-users.

In my direct testimony I summarized five proposals from the Joint CLECs. Joint CLECs first recommended that the Commission address rural ILEC access rates before addressing CLEC access rates.[3] Both Rural LECs ("RLECs") and IXCs apparently agree that RLEC access rates should be addressed. The process by which this is accomplished is complex and disagreements remain as to the best method to achieve access reductions for rural carriers. The Commission would be best served by focusing its efforts first on rural ILEC access rates.

Second, the Joint CLECs recommended that to the extent the Commission elects to implement an arbitrary benchmark (i.e. a benchmark other than cost) for CLEC access rates, the Commission should benchmark the CLEC rates to the 1999 Qwest access rates.[4] These were the rates in place in Arizona before Qwest entered into a number of voluntary access rate reductions which were contingent on complete revenue neutrality for Qwest. (For example, under the original Price Cap Plan, the revenues available to Qwest under the Cap for Basket 3 Services were increased by $5 million each year that access was reduced.) These negotiated Qwest reductions did not include any discussion of CLEC access rates and, likewise, did not include any sort of mechanism for CLECs to recover access revenue had the reductions applied to CLECs. Based upon the direct testimony

[3] Denney Direct, pp. 6-7.

[4] Denney Direct, pp. 7-8.

filed in this case, the Joint CLECs would further recommend, to the extent the Commission decides to reduce CLEC access rates at this time, the Commission should limit these reductions to terminating access rates. Parties seeking reductions in CLEC access rates focus their arguments on the CLECs' asserted monopoly with regard to terminating access. This CLEC "monopoly" argument is not supported by the parties with respect to originating access[5] and thus any benchmarking of CLEC access rates should be limited to terminating rates.[6]

The Joint CLEC's third recommendation focused on timing. To the extent the Commission elects to reduce CLEC access rates at this time, reductions should be phased in gradually to give CLECs amply opportunity to adjust business plans and update term contracts. The Joint CLECs proposed a 3 year period before reductions are implemented and then a gradual phase in over five to seven years for the actual reductions.[7] A number of parties in this proceeding recommend that CLEC rates be benchmarked to Qwest's current intrastate or interstate access rates. While the Joint CLECs do not believe this is appropriate, the Joint CLECs do note that Qwest had a period of approximately 6 years to phase in and adjust to its current intrastate access rates. To the extent the Commission does not approve the transition recommended by the Joint CLECs, the Commission should, at a

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5 AT&T witness Dr. Oyefusi is the only witness to argue LECs have a monopoly with respect to originating access. As demonstrated in this testimony his conclusion is incorrect.

6 This is discussed in more detail under the heading, "Issue 1. What carriers should be covered by access reform?"

7 Denney Direct, pp. 8-10.

minimum allow Joint CLECs the same amount of time that was provided to Qwest to phase in access rate reductions.[8]

Fourth, the Joint CLECs recommended that AUSF funds only be distributed after a demonstration of need, and contributions to the fund be derived from all providers of telecommunications services.[9]

Finally, the Joint CLECs recommended that to the extent the Commission addressed CLEC access issues, it should also address the appropriate rate for intraLATA, intraMTA calls terminated by wireless providers to LECs.[10]

II. ISSUES POSED BY THE PROCEDURAL ORDER

Issue 1. What carriers should be covered by access reform?

To The Extent the Commission Mandates Access Rates Reductions for Joint CLECs, these Reductions Should be Limited to Terminating Access Rates

[8] This is discussed in more detail under the heading, "Issue 3. What procedures should the Commission implement to achieve the desired reduction in access rates?"

[9] Denney Direct, pp. 10-12.

[10] Denney Direct, p. 12. This is also discussed in more detail under the heading, "Issue 1. What carriers should be covered by access reform?"

Q. MR. SHAND TAKES A POSITION THAT IXCS HAVE NO CHOICE WHEN TERMINATING CALLS AND THEREFORE, "THE TERMINATING ACCESS RATE FOR CLECS SHOULD BE CAPPED AT THE INCUMBENT LECS RATES."[11] PLEASE RESPOND.

A. It is significant that Mr. Shand's reasoning leads only to a proposal to cap CLECs' *terminating* access rates. Indeed, talks about the alleged monopoly power of access providers typically revolve around the observation that a *terminating* IXC does not have any (immediate) options but to *terminate* a call to the LEC, and ignore the originating access. For example, Mr. Shand's only discussion about the alleged market power in the access market consists of one phrase: "With respect to *termination* of a call to a CLECs' customers, the IXCs have no alternative but to pay the CLECs' rates to terminate calls."[12] Mr. Shand goes on to cite several passages from the FCC *CLEC Access Charge Order*, [13] none of which discuss market power in originating access.[14] Yet, Mr. Shand presents his overall recommendation for CLEC access rates, which calls for capping CLECs access rate generally, with no distinction made between originating and terminating access.[15]

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11 Direct Testimony of Wilfred Shand of behalf of Utilities Division, ACC ("Shand Direct"), p. 9.

12 Shand Direct, p. 10 (emphasis added).

13 *In the Matter of Access Charge Reform,* Seventh Report and Order and Further Notice of Proposed Rulemaking, CC Docket No. 96-262; FCC 01-146, April 27, 2001 ("*CLEC Access Charge Order*").

14 Shand Direct, pp. 10-11.

15 Shand Direct, p. 11.

Q. WHY SHOULD ORIGINATING ACCESS BE DISCUSSED SEPARATELY FROM TERMINATING ACCESS?

A. IXC's argument that CLECs have monopoly power over terminating access is based on the claim that IXCs have no alternative when terminating a call to a LEC customer.[16] However, this argument makes no sense in the context of originating access. Originating access applies when the LEC end user has chosen the IXC as its long distance provider. Because the customer of the LEC is necessarily also the customer of the IXC (this is not necessarily the case for terminating access) the IXC has the ability to set long distance prices for its customer by taking into account originating access. Since end user customers look at their total telecommunications cost when selecting a local carrier, if a LEC were to set originating access charges too high it risks losing its customer as the customer would seek a carrier that can provide a better overall pricing for its telecommunications needs.

Q. WHAT ARGUMENTS FOR CAPPING CLECS ACCESS RATES ARE CONTAINED IN MR. SHAND'S CITATIONS FROM THE FCC *CLECS ACCESS CHARGE ORDER*?

A. These citations[17] contain three substantive arguments: that (1) it is an anomaly for a "competitive" provider to enter a market by charging well in excess of the

[16] See, for example, Oyefusi Direct, p. 23.

[17] Shand Direct, pp. 10-11. I do not include in this list "non-substantive" arguments, by which I mean declaratory statement that rates are unjust and unreasonable, or that CLECs have a monopoly power.

access rate charged by the market's incumbent; (2) high access charges allow CLECs unfairly to shift their operational expenses and their network build-out expenses to IXCs; and (3) CLECs access rates are unilaterally imposed through tariffs, rather than through negotiation with a willing purchaser.

The first argument does not apply to the Joint CLECs in Arizona, because, as I also demonstrated in Table 1 of my direct testimony,[18] access rates for CLECs in this case are similar to the rates that existed for Qwest in 1999 – the approximate time frame of CLECs entry. My analysis suggests that CLECs in this case, when entering the local markets, set their access rates at the level of the incumbent (a strategy that is reverse to the "anomaly" that concerned the FCC in its *CLEC Access Charge Order*). As I noted in my direct testimony,[19] changes to Qwest's rates since 1999 were the result of a series of revenue neutral settlement agreements entered into by Qwest for Qwest's benefit. There is no justification to apply reductions agreed to by Qwest to Qwest's competitors. This is tantamount to allowing the CLECs largest competitor to directly set the CLECs rates in the market.

Because the first argument (charging rates well in excess of the incumbent at the time of competitive entry) does not apply to the Arizona situation, the second argument – that it is unfair to use high access cost to shift network built-out

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[18] Denney Direct, p. 19. This table was corrected in my reply testimony (see Table 1: Corrected). As explained the correction did not change any of the conclusions based on this table.

[19] Denney Direct, p. 49.

expense to IXCs – does not apply either. As noted by Dr. Johnson, the opposite may be the case: "[M]any of the carriers participating in this proceeding view the basic local exchange customer as the "cash cow" that should be forced to cover most of the fixed costs of the network, while other services ... like wireless carrier interconnection service and interstate switched access service – are being priced at very low levels (near zero), due to the success of their advocacy efforts before the FCC."[20]

The third argument – that CLECs access rates are imposed "unilaterally" through a tariff rather than through negotiations with a willing purchaser – is similarly weak. If CLECs *had* sufficient power to unilaterally impose any access rate, their access rates would likely have been much higher. There must be some constraints that prevented the Joint CLECs from setting their intrastate access rates at the levels of Arizona RLECs, which are significantly higher. For example, CLECs could have set their access rates at the level of Arizona RLECs. Based on Mr. Shand's exhibit WMS-1, Southwestern has a composite terminating access rate of 27.8 cents a minute, SCUTA – 21.5 cents, Frontier/White Mountain – 16.7 cents, Midvale – 14.7 cents and etc. In contrast, the Joint CLECs' composite terminating access rates are in the vicinity of 4 to 5 cents.[21]

[20] Direct Testimony of Ben Johnson on behalf of RUCO ("Johnson Direct"), p. 21.

[21] Denney Direct, p. 19 Table 1.

Q. DO OTHER PARTIES SIMILARLY ACKNOWLEDGE THAT ALLEGED MARKET POWER IN THE ACCESS MARKET IS LIMITED TO TERMINATING ACCESS?

A. Yes. For example, Ms. Eckert's (Qwest) language is very specific to *terminating* access. She addresses the issue of the alleged "bottleneck" qualities of access services on pp. 5 and 9. In both cases she justifies her claims by discussing only *termination* (and not origination) of long-distance calls. Similarly, Mr. Appleby (Sprint) justifies his statement that switched access is a "monopoly" service by explaining that "[a]ll carriers that compete against LECs in the retail market must use switched access to *terminate* non-local calls to the LECs' customers."[22] Mr. Meredith (ALECA)[23] does not address market power in switched access. Mr. Price (Verizon), while claiming that an IXC does not have a choice when originating or terminating a call, nevertheless emphasizes the terminating side by stating that CLECs possess market power "*particularly as relates to terminating* switched access service"[24] and references an academic publication for "a discussion of *terminating* access monopoly"[25] without providing a parallel reference to a source that would discuss *originating* access "monopoly." Based on my review, Dr. Oyefusi (AT&T) is the only witness who argues that an IXC

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22 Direct Testimony of James A. Appleby on behalf of Sprint ("Appleby Direct"), p. 4 (emphasis added).

23 Direct Testimony of Douglas Duncan Meredith on behalf of ALECA ("Meredith Direct").

24 Direct Testimony of Don Price on behalf of Verizon ("Price Direct"), p. 8.

25 Price Direct, p. 11 footnote 5 (emphasis added).

does not have a choice when terminating or originating a call,[26] but even he recognizes that CLEC rates are constrained when he states, "If left on their own, the CLECs have an incentive to increase access rates as much as they can."[27] Given that the Joint CLEC intrastate access rates are significantly below the intrastate access rates of other LECs in Arizona, it is clear that CLECs do not have the market power to *increase rates as much as they can.*

Q. IS IT REALLY IMPORTANT THAT AN IXC DOES NOT HAVE A CHOICE OF AN ACCESS PROVIDER WHEN IT TERMINATES OR ORIGINATES A CALL?

A. No, it is not very important that an IXC does not have a choice *at the very instance* of the call. (Arguably, when such extreme short run is concerned, many real life situations appear to be "no choice" situations.[28]) A more important question is whether an IXC has an ability to control its access cost in medium and long-run – the framework more appropriate for "market power" analysis. The answer to this question is "yes."

Parties in this case shy away from claiming monopoly power in originating access because the IXC's control over originating cost in the medium and long-run is particularly apparent: For example, for decades IXCs have been using "special

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26 Direct Testimony of Ola Oyefusi on behalf of AT&T (Oyefusi Direct), p. 23.

27 Oyefusi Direct, p. 30.

28 For example, if lost in a desert in a foreign country, my only choice may be to call for help via my AT&T Wireless phone – thus incurring international roaming charges of many dollars per minute. Yet, this lack of choice at the very instance of the call is not sufficient grounds to claim that AT&T Wireless has an "originating monopoly" in the foreign country.

access by-pass" (use of special access facilities to connect large end-users to long-distance networks) to avoid switched access charges.

More recently, since local exchange markets became open to competition, and large LECs "blended" with IXCs,[29] bundling local and long-distance service introduced a method of controlling switched access cost associated with end users of all sized and segments (not just large business customers): Currently, the most direct way for an IXC to control its access cost is to acquire the end-user as a local customer (thus, serving the end-user as both a LEC and an IXC). This is particularly effective in the CLECs markets: Most of the CLECs focus on business markets, where customer acquisition is typically pro-active: CLEC's sale representative calls potential end-users. Because LECs proactively pursue potential business customers, it is easy for a company such as AT&T (an IXC and CLEC) to selectively target business customers that are served by a LEC with relatively high switched access rates. If the LEC's access rates are really excessive in relation to the true cost of providing access, AT&T (as an example) should be able to offer the end-user a local and long-distance package that would bring access cost savings to AT&T. The higher the access rates of the LEC that originally serves the end-user, the higher competition for this end-user from competing providers of bundled local/long-distance services. In other words, when setting its access rates, the LEC recognizes that the danger of setting rates at

[29] In the sense that RBOCs entered the in-region interLATA long-distance markets and largest IXCs were bought by largest ILECs.

high levels is the higher risk of losing the end-user to competitors. As a result, competition for end-users acts as a constraint on switched access rates.

Q. DID THE FCC *CLEC ACCESS CHARGE ORDER* ACKNOWLEDGE THE SCENARIO IN WHICH AN IXC CONTROLS ITS ACCESS COST BY COMPETING FOR THE END USER IN THE LOCAL MARKET?

A. Yes. The FCC CLEC Access Charge Order said as follows:

> The Commission previously projected that, at least in the case of originating access service, IXCs would likely enter marketing alliances with LECs offering low-priced access service and would thereby be able to exert downward pressure on CLEC access rates. The Commission even raised the prospect that IXCs would themselves choose to enter the local service market as a means of exerting downward pressure on terminating rates. However, *neither of these eventualities has come to pass*, at least not to an extent that has resulted in effective downward competitive pressure on CLEC access rates.[30]

Recall that the above cited text dates back to April 2001 – the time frame that predates the mega-mergers between RBOCs and largest IXCs. As I noted in my direct testimony,[31] both of these "eventualities" previously projected by the FCC *have come to pass* as the IXC and LEC segments of the industry are now "blended" together.

Q. DO TECHNOLOGICAL DEVELOPMENTS PROVIDE ADDITIONAL MEANS FOR AN IXC TO CONTROL ITS ORIGINATING AND TERMINATING ACCESS COST?

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30 *CLEC Access Charge Reform Order*, ¶ 32 (footnote omitted; emphasis added).

31 Denney Direct, p. 38.

A. Yes. Dr. Oyefusi brings up one such development, which is VoIP technology. Dr. Oyefusi claims that interconnected VoIP providers such as Vonage (VoIP service that allow calls to and from public switched network) pay as little as $0.0007 per minute to complete calls.[32] Dr. Oyefusi fails to mention that AT&T itself for years has been using VoIP services to cut its interconnection cost. For example, AT&T (the IXC) introduced residential VoIP service similar to Vonage's service (AT&T CallVantage®) in 2004 – the year it also announced its withdrawal from stand alone consumer (residential) long-distance market.[33] While Internet news blogs reported that AT&T stopped offering AT&T CallVantage® service to new customers in 2008-2009 time frame,[34] AT&T is currently offering various other VoIP services to both residential and business customers.[35]

[32] Oyefusi Direct, pp. 18-19.

[33] See AT&T Form 10-K for 2004: "On July 22, 2004 we announced that … we would no longer be investing to actively acquire new mass market local and stand-alone long distance customers." The same 10-K form also discusses the FCC orders surrounding intercarrier compensation for VoIP traffic, including the FCC ruling against a petition AT&T filed in October 2002, "holding that our long distance phone-to-phone IP telephony services are subject to terminating access charges…. As a result of this ruling, we will begin paying terminating access charges on our long distance phone-to-phone IP telephony calls." Regarding the FCC ruling that services such as Vonage services fall within the interstate jurisdiction, AT&T's 2004 10-K form concludes that "[o]ur newer VoIP services fall within this description and as a result will be subject predominantly to FCC rules."

[34] See, for example, http://gigaom.com/2008/07/03/att-shuts-callvantage/. Indeed, the current version of AT&T CallVantage web site (https://www.**callvantage.att**.com/) appears to cater only to existing customers.

[35] See AT&T "VoIP" page (http://www.corp.att.com/voip/), which offers "High speed Voice over IP service for your home or business." It does not appear that AT&T offers these products in Arizona.

Q. DR. OYEFUSI ARGUES FOR MANDATORY REDUCTIONS TO CLECS ACCESS RATES ON THE GROUNDS THAT UNDER FEDERAL LAW IXCS CANNOT CHARGE GEOGRAPHICALLY DE-AVERAGED TOLL RATES.[36] PLEASE RESPOND.

A. First, Dr. Oyefusi admits that this federal regulation concerns interstate toll rates, and that on the intrastate side IXCs offer geographically averaged rates "as a practical matter... to enable uniformity in billing."[37] In other words, IXCs charge uniform intrastate toll rate to cut their own billing cost.

Second, Dr. Oyefusi does not see the double standard in his argument: The prohibition of geographic de-averaging of toll rates has been implemented to serve the public interest at large; apparently, the lawmakers found it appropriate to spread the burden of varying long-distance and access cost across all participants in the market. By contrast, the policies advocated by AT&T seek to have CLECs alone shoulder the burden by denying them adequate compensation for switched access services rendered.

Third, while Dr. Oyefusi complains that (the geographically averaged) AT&T toll prices in Arizona are lower than access rates of "some" Arizona LECs,[38] he fails to acknowledge that this result is a direct consequence of the geographically

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36 Oyefusi Direct, pp. 21 and 23.

37 Oyefusi Direct, p. 21 footnote 11.

38 Oyefusi Direct, p. 27.

averaged rate design.[39] When a toll price is set based on *average* cost, some data points that compose this average would be above, but others would be *below* the toll price. Indeed, if AT&T statewide toll price were set to cover access cost associated with *all* LECs, including LECs with the highest access rates, AT&T would be collecting abnormal profits from calls associated with "average" and "below average" LECs.

The Commission Should Also Establish the Terminating Rate for Intrastate, IntraMTA Wireless Calls

Q. AT&T COMPLAINS ABOUT "TREMENDOUS DISPARITIES"[40] IN INTERCARRIER COMPENSATION RATES PAID BY WIRELINE CARRIERS VERSUS WIRELESS CARRIERS THAT CREATE "COMPETITIVE ADVANTAGE FOR WIRELESS LONG DISTANCE SERVICES."[41] PLEASE COMMENT.

A. While the disparities definitely exist, AT&T's testimony fails to recognize that AT&T is likely the biggest beneficiary of this disparity as one of the two largest

[39] This result is also related to the fact that access costs constitute a large portion of overall toll cost.

[40] Aron Direct, p. 71.

[41] *Id.*

wireless carriers in the country.[42] Yet, I agree that this is a serious problem given the size of wireless industry: According to the FCC data, there are over 4.9 million wireless subscribers in Arizona,[43] and only 3.1 million wireline access lines[44] (including Qwest, other ILECs and CLECs). I estimate from the FCC minutes of use data that intrastate wireless traffic in Arizona is approximately 32 billion minutes a year,[45] while intrastate (non-local) traffic for nonQwest ILECs and CLECs is approximately 1.4 billion minutes a year.[46] Dr. Aron observed that the majority of the state belongs to the same Major Trading Area ("MTA"),[47]

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42 According to the most recent FCC report on Wireless Competition (*13th Report* in WT Docket No. 08-27 released on January 16, 2009 "*FCC 2009 Wireless Competition report*", p. 7 chart 1), AT&T was the largest wireless company nationwide with over 70 million subscribers followed by Verizon Wireless with 65 million subscribers (data for 2007). However, this ranking will likely be reversed in the more recent reports that would account for the merger between Verizon and Alltel (closed in 2009. According to the above mentioned FCC report, Alltel had over 13 million subscribers in 2007).

43 *FCC Local Telephone Competition Report* released July 2009, Table 14 (data as of June 2008). The exact number is 4,935,640.

44 *Id.*, Table 7 (data as of June 2008).

45 Calculated as the number of Arizona wireless subscribers (4,935,640; from the *FCC Local Telephone Competition Report* released in July 2009, Table 14) times average wireless minutes per month (769 minutes; nationwide data for the second half of 2007 from the *FCC 2009 Wireless Competition report*, p. 7) times 12 months times percent of intrastate minutes in wireless total minutes (71%; nationwide data for residential calling in 2007 from the *FCC Trends in Telephone Service Report* released in August 2008, Table 11.4).

46 Calculated by using annual state (non-local) Dial Equipment Minutes ("DEMs") in 2000 (the most recent year when DEM data was reported; data available at http://www.fcc.gov/wcb/iatd/neca.html, "Network Usage by Carrier") and CLECs Arizona current line counts. Specifically, total minutes is the sum of DEMs for all Arizona ILECs other than Qwest in 2000 (488,129,559) plus CLECs intrastate (non-local) minutes calculated as follows: Arizona CLECs access lines (1,128,827; data for June 2008 from the *FCC Local Telephone Competition Report*, Table 7) times Qwest's Arizona state DEMs in 2000 (2,331,630,000) divided by Qwest's Arizona USF loops in 2000 (2,932,088; NECA data available at http://www.fcc.gov/wcb/iatd/neca.html, "Universal Service Fund Data: NECA Study Results").

47 Aron Direct, p. 41 (see also map of Arizona MTAs on p 43).

meaning that the majority of the wireless intrastate traffic (32 billion a year) is subject to reciprocal compensation rates.[48]

Q. HOW ARE WIRELESS INTRAMTA RECIPROCAL COMPENSATION RATES DETERMINED?

A. While the Commission has jurisdiction over these rates,[49] it is my understanding that the Commission has not addressed these rates in a systematic fashion.[50] These rates are typically set in bilateral interconnection agreements between wireless and landline carriers – *if* there is an interconnection agreement, which is not always the case. Unfortunately, wireless carriers have refused to negotiate an agreement, in which case the exchange of traffic is not compensated. Integra has faced difficulty negotiating contracts with certain wireless carriers. This issue likely affects not only Integra, but other CLECs and ILECs in Arizona. As noted above, wireless market is significantly bigger than wireline market, and the traffic is not in balance, meaning that a "bill and keep" arrangement does not provide fair compensation to a wireline carrier.

A local exchange company cannot refuse to terminate wireless traffic. Therefore, in order to get fair compensation for terminated traffic its only option is to litigate the case. Litigation is costly and inefficient not only for litigating carriers, but also for the Commission (given the potential number of pairs "LEC-wireless

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48 Aron Direct, p. 73 and Appleby Direct, p. 8.

49 See my direct testimony, Denney Direct, p. 22.

50 The Commission set reciprocal compensation rates for Qwest in cost docket No. T-00000A-00-0194. These rates would apply in situations involving termination to Qwest end users.

carrier"). Therefore, it makes sense for the Commission to set default termination rates for wireless intraMTA traffic. Because the Joint CLECs propose that if the Commission mandates CLECs access rate reductions, these reductions should be based on cost,[51] it is only logical that the Joint CLECs default rates for intraMTA traffic termination be set at the same (cost-based) switched access level. Under this design the rate for intraMTA traffic would be the same as the rate for terminating intrastate switched access traffic, meaning that the "playfield" would be leveled for wireless and wireless ling-distance services.

Q. PLEASE SUMMARIZE YOUR TESTIMONY ON INTRAMTA WIRELESS TRAFFIC.

A. Wireless intraMTA traffic in Arizona is by an order of a magnitude larger than intrastate switched access traffic of ILECs and CLECs taken together. If the Commission wishes to "create a level playing field for all companies in Arizona"[52] and/or address the "competitive advantages of wireless long distance services,"[53] the Commission should do so by tackling the five hundred pound gorilla in the room – rates for intraMTA wireless termination over which it has jurisdiction. The Commission should clarify that local exchange carriers are entitled for compensation for intraMTA traffic from wireless carriers, and set default compensation rates.

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51 Denney Direct, p. 8.
52 Eckert Direct, p. 7.
53 Aron Direct, p. 71.

Issue 2. To what target level should access rates be reduced?

Any Target Other Than The Carrier Cost is Arbitrary

Q. HAS ANY PARTY PRESENTED ACTUAL EVIDENCE THAT CLEC ACCESS RATES ARE EXCESSIVE?

A. No, there has been no substantive evidence presented in this proceeding that CLEC access rates are excessive or are not just and reasonable. The only "evidence" that parties typically cite (without regard to a particular group of carriers) are the generic complaints that intrastate access rates are higher than interstate rates.[54] However, as correctly noted by Staff's Mr. Shand, "[i]nterstate access charges are generally lower than intrastate access charges because of the manner in which costs that have been allocated to interstate access are recovered."[55] Here Mr. Shand refers to the monthly federal Subscriber Line Charge ("SLC") that the FCC instituted to recover certain interstate access cost (often referred to as "non-traffic-sensitive" cost) – a charge that is collected from an end-user, rather than an IXC. Currently, Qwest's federal SLC in Arizona is $6.20 per line per month.[56] When combined with Qwest's Arizona total interstate access volumes and access lines, this SLC translates into a 2.6 cents charge per

[54] Aron Direct, p. 83. Oyefusi Direct, pp. 18-19.,

[55] Shand Direct, p. 4.

[56] Qwest's Tariff FCC No. 1, section 4.7.1.

minute.[57] In other words, because the state access rate structure is different from the interstate rate structure, to properly compare Qwest's interstate and intrastate access rates, 2.6 cents per minute should be added to the interstate rate. Incidentally, because Qwest's composite intrastate access rate is believed to be around 2.22 cents,[58] it follows that Qwest's composite interstate access rate (when recalculated on a per minute basis) is higher than its intrastate rate.

Q. TO CLARIFY YOUR LAST POINT: IF QWEST'S INTERSTATE SLC SWITCHED ACCESS RATE IS CONVERTED TO A PER MINUTE BASIS, WHAT WOULD BE QWEST'S COMPOSITE INTERSTATE ACCESS RATE?

A. According to the FCC, Qwest's composite interstate access rate without SLC is 0.99 cent per minute, which includes both traffic sensitive (per minute) and non-traffic sensitive (per month) charges other than SLC.[59] When SLC (2.6 cents per minute) is added to this number, Qwest's total composite interstate switched access rate on a per minute basis is **3.57 cents**.

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[57] Calculated as $6.20 divided by Interstate Access Minutes per Month per Line (which is Total Annual Interstate Access Minutes (5,422,374,736) divided by USF Loops (1,910,999) divided by 12 months, resulting in 240 minutes per month per line). Minutes and USF Loops data are for 2008 contained in NECA submissions and available at http://www.fcc.gov/wcb/iatd/neca.html , "Network Usage by Carrier" and "Universal Service Fund Data: NECA Study Results."

[58] Shand Direct, p. 19.

[59] Source: the FCC 2009 Monitoring Report, Table 7.10, data for Qwest's 14-state territory, rates effective between July 2009 and June 2010. Traffic sensitive portion is 0.79 cents, and non-traffic sensitive portion is 0.20 cents per minute. Note that the resulting aggregate rate (0.99 cents per minute = 0.79 + 0.20) is consistent with AT&T estimates for Qwest Arizona contained in highly confidential Figure 1 of Aron Direct, p. 10.

Q. SHOULD THE COMMISSION ALTER THE INTRASTATE ACCESS RATE STRUCTURE TO INSTITUTE A PER LINE PER MONTH CHARGE SIMILAR TO THE FEDERAL SLC?

A. No. Just because the FCC instituted this manner of cost recovery does not mean that the Commission should follow suit. As correctly noted by Dr. Johnson,[60] the majority of non-traffic sensitive cost is what he calls "joint cost" – cost of facilities shared by several services. Dr. Johnson discusses local loop as a typical example of a "joint cost" facility – facility that is used by both local and toll service.[61] He concludes that "[i]t makes no economic sense to impose the entire cost of the access line, as part of the price of local service, on the particular end user who requests installation of the line. Rather, it is appropriate to recover the cost from all of the beneficiaries of that line--including the other local customers in that city and the toll carriers that also benefit from the new line...."[62] In other words, just like my direct testimony,[63] Dr. Johnson expresses an opinion that IXCs/toll services should pay for the use of local loop that makes their services possible.

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60 Johnson Direct, pp. 26-28.

61 *Id.*, pp. 27-28.

62 *Id.*, p. 28.

63 Denney Direct, pp. 61-63.

Further, as I explained in my direct testimony,[64] current interstate rates were not established based on cost, but were a result of negotiations where concessions on unrelated issues were traded for access reductions.

Q. DR. OYEFUSI CLAIMS THAT INTERSTATE RATES ARE GREATER THAN COST BECAUSE THE FCC'S COST BASED RATE IS $0.0007.[65] IS THIS CORRECT?

A. No. The $0.0007 referred to by Dr. Oyefusi came out of the FCC's ISP Remand Order.[66] The rate established by the FCC was not for interstate access traffic, but dial up ISP traffic[67] and was not based on a cost study, but instead based upon a rates agreed to by Level 3 as part of agreements with AT&T.[68] Further, the FCC recognized that carriers cost to deliver ISP traffic may exceed the $0.0007 rate[69] and specifically found "These rates do not, therefore, reflect the costs incurred by any particular carrier for providing service to a particular customer."[70]

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64 Denney Direct, pp. 31-33.

65 Oyefusi Direct, p. 44.

66 In the Matter of Implementation of the local Competition Provisions in the Telecommunications Act of 1996 and Intercarrier Compensation for ISP-Bound Traffic, CC Docket No. 96-98 and CC Docket No. 99-68, Order on Remand and Report and Order ("ISP Remand Order"), released April 27, 2001.

67 *ISP Remand Order,* ¶ 1.

68 *ISP Remand Order,* ¶ 85.

69 *ISP Remand Order,* ¶ 80.

70 *ISP Remand Order,* ¶ 77.

Q. DR. ARON REFERS TO RECIPROCAL COMPENSATION RATES AS "EVIDENCE" THAT INTRASTATE SWITCHED ACCESS RATES ARE TOO HIGH.[71] PLEASE RESPOND.

A. Reciprocal compensation is not a good "benchmark" for CLECs and RLECs access rates for a number of reasons. First, reciprocal compensation involves two-way/mutual exchange of local traffic between two local exchange carriers. If the traffic is in balance, it does not matter whether the reciprocal compensation is zero or, as an example, 30 cents per minute. Because the exchange is directed both ways, often carriers agree to low or zero (bill and keep) rates. In contrast, switched access involves "one-way" exchange in the sense that an IXC (an intermediary) is using networks of two local exchange carriers. In the case of reciprocal compensation for local traffic there is no intermediary carrier and therefore, as an example, there is no need to allocate the cost of local loop between "local" and "access" services (because only local service/local carrier uses the loop during local call).

Further, reciprocal compensation is not a good "benchmark" for access rates because there may be cost differences between the provision of local call termination and access services. For example, from Qwest's UNE cost models we know that Qwest uses different traffic measurement/billing systems (with

[71] Aron Direct, p. 83.

different per minute cost) for access and local traffic.[72] Other factors that drive cost differences between access and local traffic include call duration and trunk utilization. Finally, while Qwest's reciprocal compensation rates were indeed established based on an investigation of its cost, these rates have nothing to do with the cost incurred by *other* carriers (CLECs and RLECs) in Arizona.

Q. YOUR DIRECT TESTIMONY SUGGESTED THAT IF THE COMMISSION DECIDES TO REVIEW CLECS ACCESS RATES, THE STANDARD FOR THIS REVIEW SHOULD BE EACH CLEC'S COST. DO ANY PARTIES PROVIDE TESTIMONY IN SUPPORT FOR THE NOTION THAT COST IS THE MOST APPROPRIATE STANDARD?

A. Yes. Mr. Shand proposes that CLECs have an option of filing a cost study if they believe their cost is higher than the ILEC's cost (at which rates CLECs would be capped under Mr. Shand's proposal).[73] Dr. Aron justifies AT&T proposal of reducing intrastate rates to the level of interstate rates by saying that this proposal would bring intrastate rates closer to cost.[74] Ms. Eckert (Qwest) provides examples of states that cap CLECs access rates.[75] As seen from Ms. Eckert's citations to state rules,[76] Connecticut, New York and Pennsylvania rules include such cost justification of higher rates. Similarly, California rules also allow

[72] See, for example, the ongoing Colorado docket No. 07A-211T, Qwest's March 4, 2009 filing, Direct Testimony of Christopher Viveros on behalf of Qwest, Exhibit CV-9, which contains Qwest's local interconnection usage (reciprocal compensation) study.

[73] Shand Direct, p. 11.

[74] Aron Direct, pp. 82-83.

[75] Eckert Direct, pp. 8-9.

[76] Eckert Direct, pp. 8-9.

CLECs to justify rates in excess of the established benchmark (which is 10% over the higher of SBC or Verizon's rates) by using the CLEC's actual cost.[77] According to Mr. Price,[78] Nebraska is another example of a state that, while regulating CLECs access rates, also permits them to charge cost-justified rates. While it is not captured in Mr. Price's citations to state rules, Massachusetts (which is on Mr. Price's list of states that cap CLECs access rates) also allows exemption from the cap on CLEC access rates based on a cost showing.[79] In general, regulators' efforts to reform intercarrier compensation rates have been aimed at bringing rates closer to cost (not further from cost). For example, just last month the FCC Commissioner Clyburn said "Intercarrier compensation reform should include harmonizing interstate and intrastate interconnection rates, and those rates should be just and reasonable and *reflect the actual costs to use the networks*."[80]

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77 See California Public Utilities Commission Decision 07-12-020 in Rulemaking 03-08-018 dated December 6, 2007, 2007 Cal. PUC LEXIS 609, *24: "The Commission may authorize intrastate access charges higher than these caps upon a showing, supported by a detailed cost-of-service study, that a competitive carrier's actual costs exceed the caps adopted in today's decision."

78 Price Direct, p. 16.

79 See Massachusetts Department of Telecommunications and Cable, D.T.C. 07-9 Order On Motion For Reconsideration And Clarification dated December 7, 2009, p. 21: "a CLEC will be subject to the rate cap (once effective) unless and until the Department determines, based on a cost filing, that it is reasonable for the CLEC to charge switched access rates above the rate cap."

80 See Prepared Remarks of FCC Commissioner Mignon L. Clyburn, OPASTCO's Winter Meeting, San Diego, CA, January 25, 2010 (emphasis added).

Q. HAS VERIZON ARGUED THAT ACCESS RATE REDUCTIONS NOT BASED ON A CARRIER'S COST ARE CONFISCATORY AND THUS ILLEGAL?

A. Yes. Verizon recently filed for a stay of the New Jersey Board of Public Utilities decision to "dramatically reduce [Verizon's] access charges."[81] Verizon argues that a LEC must be permitted to "recover the costs it incurs to provide [regulated] services, along with a constitutionally adequate return of and on investments needing to provide such services."[82] Verizon argues that a regulator cannot look to services in an unregulated, competitive market in order to "ensure that those services produce a sufficient return to make up for any shortfall from the services the regulator does control."[83] In other words, Verizon is saying that it would be inappropriate for a commission to set CLEC access rates below cost and expect CLECs to pass those rate reductions onto its customers in the competitive retail market. A copy of Verizon's request is attached to this testimony as exhibit DD-1.

81 In the Matter of the Board's Investigation and Review of Local Exchange Carrier Intrastate Exchange Access rates, BPU Docket No. TX08090830, Emergent Application for a Stay of the Board's Access Charge Order, ("Verizon Stay Request"), February 3, 2010, p. 1.

82 *Verizon Stay Request*, p. 1.

83 *Verizon Stay Request*, p. 4.

If Cost is Not Used to Set Access Rates, then for CLECs Competing in the Qwest Territory, Qwest's 1999 Access Rates Should be Used

Q. YOUR DIRECT TESTIMONY PROPOSED THAT IF THE COMMISSION ELECTS TO ESTABLISH A BENCHMARK FOR CLEC ACCESS RATES OTHER THAN COST, THE BENCHMARK SHOULD BE QWEST'S INTRASTATE ACCESS RATE FOR 1999. DID OTHER PARTIES' DIRECT TESTIMONY CONTAIN ANY SUPPORT FOR THIS PROPOSAL?

A. Yes. Dr. Aron, when discussing the FCC 2001 *CLEC Access Charge Order* that capped CLECs interstate access rates, provides the following citation from ¶ 37 of this order:

> [The FCC found] persuasive the IXC arguments that it is highly unusual for a competitor to enter a market at a price dramatically above the price charged by the incumbent, absent a differentiated service offering.[84]

The significance of the above citation is that the argument that persuaded the FCC was focusing on price differentials between the incumbent and competitive carriers *at the moment of entry.* This citation is consistent with my proposal to use Qwest's 1999 intrastate switched access rates as a benchmark for CLEC rates: As I explained,[85] the 1999 time frame was the time period when most CLECs were

[84] Aron Direct, p. 87.

[85] Denney Direct, p. 49.

entering the competitive market. These rates would have been considered when CLECs made the determination on whether they could enter and compete in local markets. Further, the Qwest access rates in 1999 time reflected the price Qwest thought it needed to charge for access, before buying down that price with a subsidy from revenue earned from other services (Basket 3 services). The changes which followed to Qwest's access rates were the result of a series of revenue neutral settlement agreements entered into by Qwest for Qwest's benefit – changes that CLECs cannot (on the revenue side) mimic. I also noted that most CLECs have rates that are similar to the rates that existed for Qwest in 1999.[86]

Issue 3. What procedures should the Commission implement to achieve the desired reduction in access rates?

Reduction in Access Rates Should be Implemented Gradually to Allow LECs Adequate Opportunity to Adjust Their Business Plans

Q. YOUR DIRECT TESTIMONY PROPOSED THAT IF THE COMMISSION DECIDES TO MANDATE ACCESS RATE REDUCTIONS FOR CLECS, THE TRANSITION PERIOD SHOULD BE AT LEAST 8 TO 10 YEARS.[87] DO ANY PARTIES ADDRESS THE DANGERS OF SUDDEN CHANGES IN RATES AND COST SHIFTING?

86 Denney Direct, p. 49.

87 Denney Direct, p. 13.

A. Yes. Dr. Johnson comments on the dangers of sudden rate changes throughout his testimony. For example, Dr. Johnson states, "the arguments in favor of drastic cost shifting tend to be inconsistent with both economic theory and common sense."[88] Dr. Johnson addresses the issues of sudden rate changes as harmful to competition by noting as follows: "it is also important to carefully evaluate the potential consequences of proposed realignments of telecommunications prices at this stage in the effort to transition toward a more competitive market. While reducing access rates may benefit some carriers, the policy changes being advocated in this case won't necessarily help new entrants gain a foothold in the market, and there may be unintended consequences of such a policy, which may make further progress towards effective competition less likely to be achieve in some markets."[89]

Q. THE PARTIES GENERALLY PRESUME THAT CLECS CAN INCREASE THEIR END-USER PRICES TO COMPENSATE FOR MANDATED ACCESS RATE REDUCTIONS.[90] IS IT AN ACCURATE PRESUMPTION IN ARIZONA?

A. No. First, as I noted in my direct testimony, CLECs are small carriers (when compared to Qwest, their incumbent competitor) operating in competitive end-

88 Johnson Direct, p. 8.

89 Johnson Direct, p. 25.

90 For example, Mr. Price (Verizon) claims on p. 4 that "CLECs already have unfettered retail pricing flexibility because they are not subject to rate regulation and may price their retail services as they wish."

user markets, and therefore, are *price takers in the end-user markets.*[91] As such, CLECs cannot simply offset ordered access rate reductions by a "revenue neutral" increase in their end-user local rates because their biggest competitor, Qwest, would not be subject to access rate reductions and therefore, would not be increasing local rates. Competitive markets mean that all carriers (CLECs and the ILEC, Qwest) charge essentially the same "market rate." If the current market rate for local business line is $25 per line per month (as an example), but tomorrow the Commission mandates CLECs access rate reductions, CLECs would not be able to compensate lost access revenues through higher local rates: A CLEC cannot charge a rate of $30 per line per month because its end-users would simply migrate to Qwest (who continues to offer the rate of $25 per line per month). Dr. Oyefusi recognizes this when he testifies, "CLECs did not and do not have market power in retail local services…"[92]

Second, I also explained in my direct testimony that CLECs serve primary business markets and typically have long-term contracts with their business customers.[93] Because the prices that CLECs charge end-users are typically fixed for the term of the end-user agreement, CLECs may not be able to immediately increase end-user prices for existing term customers to compensate for lost access revenue.

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91 Denney Direct, p. 9. I am stressing here "end-user market" to clarify that the issue of the alleged market power in the access markets is not important here.

92 Oyefusi Direct, p. 23.

93 Denney Direct, p. 52.

Third, contrary to the claims of Mr. Price that "CLECs already have unfettered retail pricing flexibility because they are not subject to rate regulation and may price their retail services as they wish,"[94] Arizona-specific rules do not allow CLECs to simply increase their end-user rates as they wish. Instead, CLECs end-user services are tariffed, and the rates are subject to maximum ceilings contained in these tariffs.[95] In order to increase the maximum ceiling, a CLEC would have to obtain permission from the Commission. Before the CLEC can file the application to obtain this permission, it must notify customers of the planned rate increase. In other words, even if the Commission permits to increase in maximum rates, obtaining the permission will take time given that the Commission may request additional information, and could schedule a hearing on the rate increase.[96]

Q. WHAT WAS THE LENGTH OF THE TRANSITION PERIOD IN QWEST'S INTRASTATE ACCESS RATE REFORM?

A. Qwest had a period of approximately six years to reduce intrastate access rates to their current levels. Over this time period Qwest made four reductions in intrastate access rates.

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94 Price Direct, p. 4.

95 See Arizona Rule R14-2-1109.

96 See Arizona Rule R14-2-1110.

During the 1999 price cap docket[97] Qwest entered into a settlement in October 2000 to reduce intrastate access rates. This settlement was approved on March 30, 2001 and rate reductions took place in three equal steps over a three year period beginning April 1, 2001.[98] Qwest agreed to further access reductions as part of a settlement in the 2003 price cap docket.[99] This settlement was filed in August 2005 and the Commission approved the settlement on March 23, 2006. Access rate reductions took effect on April 1, 2006. If the Commission decides to mandate CLECs access rate reductions, the transition period applicable to CLECs should be no shorter than Qwest's transition period.

Issue 4. Should carriers be permitted to contract for access rates that differ from their tariffed rates?

Carriers Should be Required to Pay Tariff Access Rates

97 In the Matter of the Application of U S WEST Communications, Inc. for a Hearing to Determine the Earnings of the Company for Ratemaking Purposes, to fix a Just and Reasonable Rate of Return thereon and to Approve Rate Schedules, Docket No. T-01051B-99-0105, Opinion and Order, ("1999 Price Cap Order"), March 30, 2001.

98 Qwest was able to make revenue-neutral rate increases to offset the access reductions. See Denney Direct, pp. 20-21.

99 In the Matter of Qwest Corporation's Filing of Renewed Price Regulation Plan, Docket No. T-01051B-03-0454, Opinion and Order, ("2003 Price Cap Order"), March 23, 2006.

Q. MR. SHAND PROPOSES TO ALLOW CONTRACTS BETWEEN CLECS AND IXCS THAT CONTAIN LOWER THAN TARIFFED ACCESS RATES. MR. SHAND PROPOSES THAT THESE CONTRACTS ARE FILED WITH THE COMMISSION AND BE AVAILABLE TO SIMILARLY SITUATED CARRIERS.[100] PLEASE RESPOND.

A. First, the Commission should clarify that IXCs are required to pay tariffed access rates. The Commission must affirm that IXCs are prohibited from engaging in self help (*i.e.*, withholding payments for access charges based on filed rates) as a means of forcing a CLEC to "agree" to reduce rates for that IXC. Second, LECs should be allowed to enter into contracts for rates that differ from the tariffed rates. Further, the Joint CLECs are not opposed to Mr. Shand's proposed requirement that contracts containing rates that differ from tariffed rates be filed with the Commission.

Issue 6. How much of access cost recovery, if any, should be shifted to end users? What showing should be required for such a shift? What should be the role of "benchmark" rates and how should benchmarks be set?

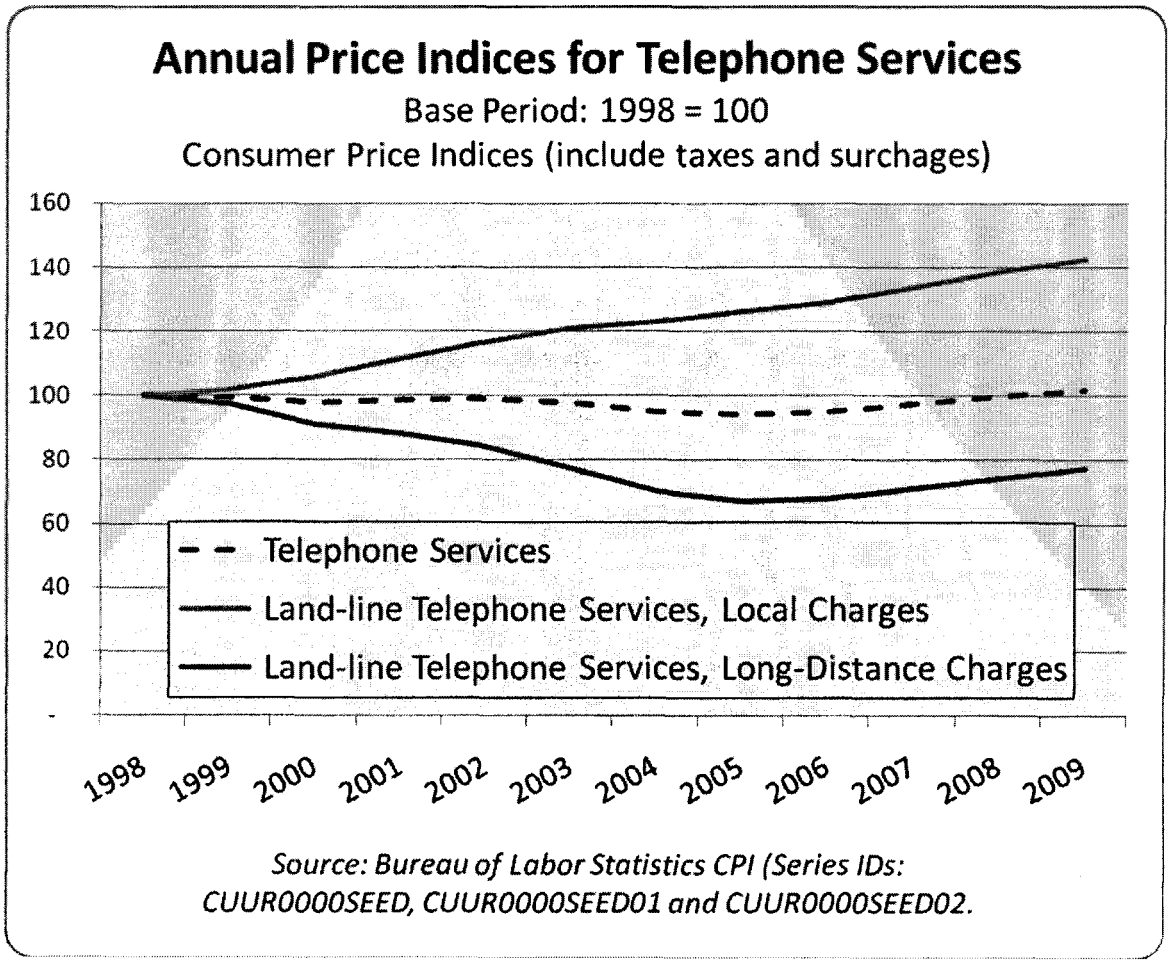
AT&T Projections of the Alleged End User Savings from Access Rate Reductions are Overstated

[100] Shand Direct, pp. 3-4.

Q. DR. ARON PRESENTS VARIOUS DATA[101] INTENDED TO CONVINCE THE COMMISSION THAT ACCESS RATE REDUCTIONS WOULD NECESSARILY TRANSLATE INTO LOWER TOLL PRICES AND SAVINGS TO END USERS. PLEASE COMMENT.

A. While I do not dispute that there is a correlation between access rates and toll prices, I do not agree that this correlation would necessarily bring savings to Arizona end users. There are a number of flaws in Dr. Aron's analysis that result in a misleadingly optimistic picture of consumer benefits from the envisioned access reductions. First of all, Dr. Aron's analysis neglects to account for **increases in local service charges and USF surcharges** that would be necessary to replace lost access revenue. If historical changes in toll prices are looked at next to historical changes in local rates and surcharges, it becomes clear that the two are part of a "zero-sum game." The following chart, which depicts Consumer Price Indices ("CPIs") of Local and Long-Distance telephone service nationwide, as well as telephone service in aggregate, makes this point:

[101] Aron Direct pp. 55 – 67.



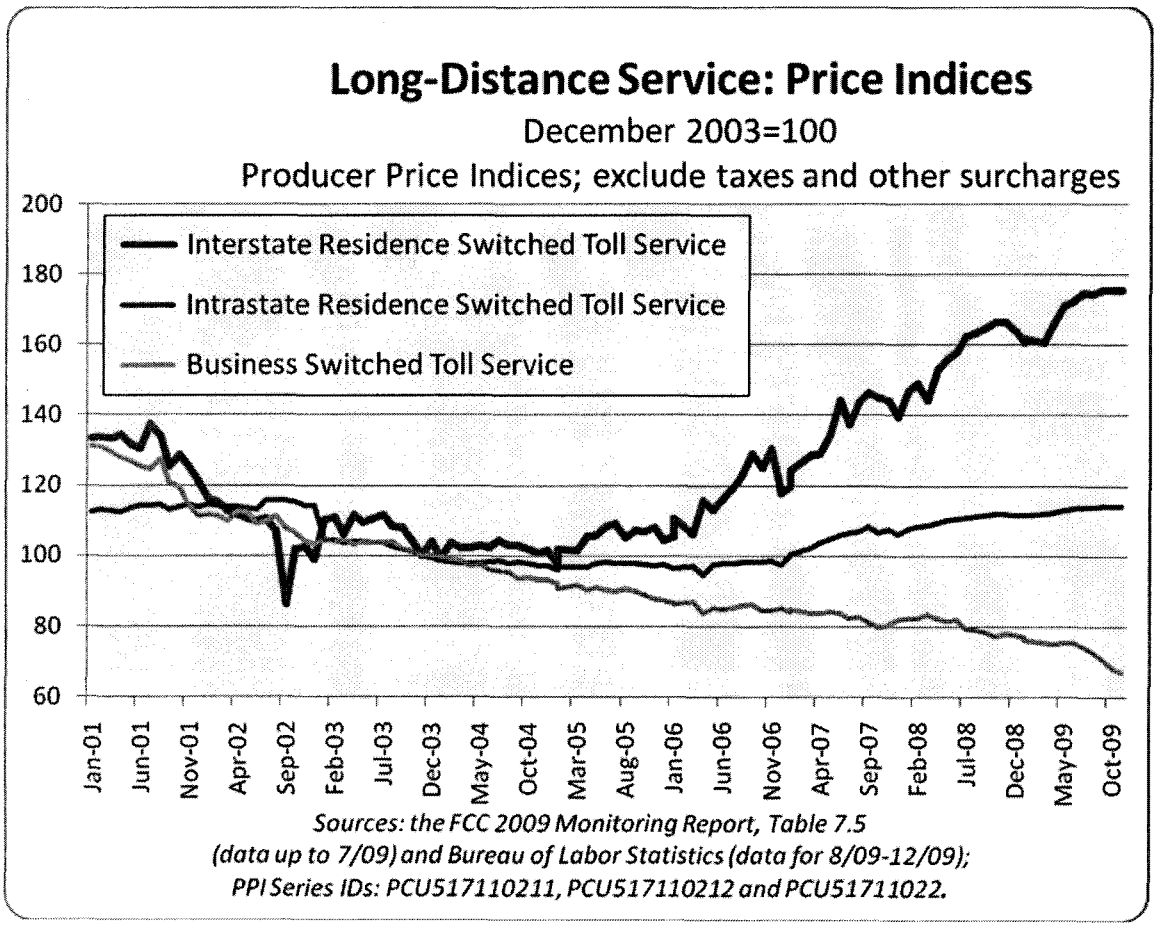
As shown in the above chart, while toll prices have been falling in the last ten years, local service prices have been increasing, and the price index of "aggregate" telephone service was relatively stable. Therefore, while access rate reductions may bring savings to *long-distance* customers, local customers (many

of which would not be the same as long-distance customers) would see increases in their local service expenditures.[102]

The second flaw in Dr. Aron's analysis is that she does not separate residential markets from business markets. Recent price trends in residential and business markets have been quite different (despite the fact that the same access rates apply to business and residential calls), as can be seen from the toll price index data collected by the U.S. Bureau of Labor Statistics ("BLS").[103] These data are presented in the following chart:

[102] Dr. Aron attempts to address this issue on pp. 97-98 of her testimony by citing an old academic paper that examined the dynamics of telephone penetration rates, local and toll prices between 1984 and 1990. According to Dr. Aron, this paper found that "rate rebalancing" (between toll and local prices) resulted in increased telephone penetration during the period studied (1984-1990). While this result may indeed have been *suggested by* the old data, its relevance to current markets is highly questionable because of the drastic changes in toll prices that happened since that time. Specifically, based on the FCC data (the FCC 2008 *Trends in Telephone Service Report*, Table 13.4), while current (2006) Average Revenue per Minute ("ARPM") for interstate and international calls is around 7 cents, it was 30 cents in 1984 (when measured in then-current dollars; this is equivalent to 63 cents a minute when measured in 2006 dollars) and 20 cents in 1990 (or, equivalently, 31 cents in 2006 dollars). It is unreasonable to draw parallels between one market where a price dropped from 63 to 31 cents a minute and another market where the initial price is only 7 cents.

[103] Here I use the BLS's Producer Price Indices ("PPIs") rather than Consumer Price Indices because the former exclude taxes and surcharges, and as such, present a more appropriate measure of "raw" toll prices.



As captured in the chart above, interstate residential toll prices increased between the end of 2003 (the "baseline" period in the BLS data for which the index is set to 100) and present by almost 1.8 times.[104] Yet, as shown in Dr. Aron's Figure 5 on page 59,[105] interstate access rates have been roughly at the same level since

[104] The index for December 2009 is 175.6, which, as all BLS price indices, is a preliminary measure subject to revisions four months after its initial publication. The most recent "non-preliminary" index is for August 2009, which is 174.9.

[105] As a side note, there must be an error in Dr. Aron's chart. Dr. Aron's chart shows that the interstate long-distance price (Average Revenue per Minute ("ARPM")) dropped in 2006. However, a review of the referenced source of the data on this chart (Table 13.4 of the FCC 2008 *Trends* Report) shows that this data point is incorrect, and the ARPM in 2006 should be at the same level as the ARPM in 2005 ($0.06). Further, the more recent FCC *Monitoring Report* for 2009, Table 7.6 contains the ARPM data on interstate calls for 2007, which is $0.07 per minute.

2003. Clearly, the dramatic increases in interstate residential toll prices between 2003 and present cannot be explained by changes in interstate access rates.

Further, the above chart shows that while intrastate residential toll prices also increased, rates for business toll service have been falling. Therefore, combining residential and business toll markets into one measure (as done in Dr. Aron's analyses) would create a misleading appearance of relatively stable[106] toll rates.

The distinction between residential and business toll market is important because of the different levels of competitive pressures (incentive to decrease price) that exist in these markets. Arguably, competition in residential markets in Arizona is significantly smaller than competition in business markets.[107] Weaker competitive pressures mean that long-distance carriers have fewer incentives to pass through their access cost savings to residential end-users.

The third flaw in Dr. Aron's analysis is that her regression-based projections of alleged consumer savings (19 to 42%[108]) do not account for the manner in which AT&T sets its long-distance pricing. As I noted in my direct testimony,[109] in residential markets AT&T offers the *same* in-state calling plans in different states

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106 Current price index for the combined business and residential toll service is only 110, or, equivalently, 1.1 times higher than this index at the end of 2003 (see BLS Index for "Public Switched Toll Service", series ID PCU5171102, data for December 2009). This result is due to the fact that business segment of toll market is larger than the residential segment.

107 According to the FCC 2008 *Trends Report*, Table 9.6, in 2007 (the most recent data available), Qwest dominated the long-distance residential market in the West (its 14-state serving territory) with 46.9% share in intraLATA direct-dialed minutes and 53.8% share in direct-dialed interLATA minutes. AT&T share in both segments was 2.2 and 2.1% correspondingly.

108 Aron Direct, p. 65.

109 Denney Direct, pp. 64-65.

(such as the "10 cents a minute plan with a $2.99 monthly fee"[110]), with the only difference between states being an "in-state connectivity fee," which is currently $1.49 per month in Arizona. Therefore, unless AT&T abandons its practice of uniform (across states) pricing, Arizona's residential consumers can at most expect an elimination of the in-state connectivity fee ($1.49 per month). However, this maximum savings is the *upper boundary* and is likely too optimistic because, as I noted in my direct testimony, even in "low access cost" states such as Nebraska AT&T has the in-state connectivity fee, and this fee in Nebraska is even higher than the Arizona in-state connectivity fee. [111]

Q. DO YOU HAVE ANY OTHER COMMENTS ABOUT DR. ARON'S FORECAST OF ARIZONA TOLL PRICE REDUCTIONS STEMMING FROM AT&T PROPOSED ACCESS RATE REDUCTIONS?

A. Yes. Dr. Aron makes this forecast based on the nationwide data of intrastate toll and access rates depicted in her Highly Confidential Figure 6.[112] Dr. Aron provided the underlying data for Figure 6 in response to Joint CLEC Discovery Request 1.1.[113] This data set – while appropriate in an academic study, is too broad for the specific purpose of this case (evaluating proposals to reduce access rates) as it includes a large number of observations for which intrastate access

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110 See AT&T web site at http://www.shop.att.com/plancomparison.jsp.

111 *Id.*

112 Aron Direct, p. 61.

113 This data set contains annual observations for 50 states between 2004 and 2008. Dr. Aron's regression model assumes that access cost affect toll rates with a lag of one year. As a result, Dr. Aron's regression data set contains in a total of 200 observations (=50 states times four years of data).

costs are significantly higher than Arizona access rates. Much more appropriate for this case is the examination of data points that correspond to "low" access rates. Specifically, because AT&T's proposal is to set Arizona intrastate rates at interstate rates,[114] Dr. Aron's analysis should have focused on data points that approximate AT&T's proposal. Based on Dr. Aron's Highly Confidential Figure 7,[115] AT&T interstate per minute access cost in Arizona is slightly under *****BEGIN HIGHLY CONFIDENTIAL [redacted] END HIGHLY CONFIDENTIAL*****. Examination of Dr. Aron's intrastate toll and access rates data underlying her Highly Confidential Figure 6 shows that currently[116] *****BEGIN HIGHLY CONFIDENTIAL [redacted] END HIGHLY CONFIDENTIAL***** intrastate access rates[117] as low as AT&T's proposal. Further, while there *****BEGIN HIGHLY CONFIDENTIAL [redacted] END HIGHLY CONFIDENTIAL***** out of 200 observations in Dr. Aron's data set for which intrastate access cost is below the AT&T proposal for Arizona, toll rates that correspond to *****BEGIN HIGHLY CONFIDENTIAL [redacted]**

[114] Oyefusi Direct, p. 4.

[115] Aron Direct, p. 63.

[116] Here "currently" means the most recent data point in Dr. Aron's data set, which is year 2008.

[117] Here "intrastate rates" mean AT&T average intrastate access cost contained in the data underlying Figure 6 that was provided in response to Joint CLEC Discovery Request 1.1.

END HIGHLY CONFIDENTIAL* are not that different from Arizona toll rates, especially when considering the difference in access costs.[118]

Q. A NUMBER OF PARTIES, INCLUDING STAFF,[119] VERIZON[120] AND ALECA[121] PROPOSE THAT ALL INTRASTATE ACCESS RATES BE SET TO OR CAPPED AT QWEST'S INTRASTATE ACCESS RATES. CAN YOU EVALUATE THIS PROPOSAL BASED ON DR. ARON'S NATIONWIDE INTRASTATE TOLL AND ACCESS RATE DATA THAT UNDERLY HER FIGURE 6?

A. Yes. Qwest's composite intrastate access rate in Arizona is believed to be $0.022.[122] Based on Dr. Aron's data set of nationwide access and toll rates, there are ***BEGIN HIGHLY CONFIDENTIAL [redacted] END HIGHLY CONFIDENTIAL*** observations (out of 200) with intrastate access rates at or below Qwest's Arizona intrastate access rates. The average intrastate toll price that correspond to these observations is ***BEGIN HIGHLY CONFIDENTIAL [redacted] END HIGHLY CONFIDENTIAL***, which is very close to Arizona's current intrastate toll price of ***BEGIN HIGHLY CONFIDENTIAL [redacted] END HIGHLY CONFIDENTIAL***. In other

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118 Toll rates were as follows: ***BEGIN HIGHLY CONFIDENTIAL [redacted] END HIGHLY CONFIDENTIAL***. Year 2008 is the most recent data point.

119 Shand Direct, p. 26.

120 Price Direct, p. 3.

121 Meredith Direct, p. 7.

122 Shand Direct, p. 19.

words, while there are states with intrastate access rates that are capped as low as Qwest's Arizona intrastate access rates, intrastate toll prices in these states are on average the *same* as intrastate toll prices in Arizona (and in a number of these states – higher than toll prices in Arizona) – which further highlights my point that Dr. Aron's projected savings to long-distance customers from the proposed access reductions are highly doubtful.

Q. DOES THIS CONCLUDE YOUR TESTIMONY?

A. Yes.

EXHIBIT

DD-1

STATE OF NEW JERSEY
BOARD OF PUBLIC UTILITIES

In the Matter of the Board's Investigation and Review of Local Exchange Carrier Intrastate Exchange Access Rates	)	**BPU DOCKET NO. TX08090830**

EMERGENT APPLICATION FOR A
STAY OF THE BOARD'S ACCESS CHARGE ORDER

INTRODUCTION

Verizon New Jersey Inc. ("Verizon NJ") respectfully requests that the New Jersey Board of Public Utilities (the "Board") stay enforcement of its Order issued February 1, 2010 in this docket ("Access Charge Order"), pending judicial review. Because the Access Charge Order would require Verizon NJ to dramatically reduce its access charges by February 21, 2010, Verizon seeks emergency relief and asks the Board to decide this application no later than February 5, 2010. Absent receiving a stay of enforcement of the Access Charge Order by February 5, 2010, Verizon NJ intends to seek a stay from a court of competent jurisdiction pending its review of the Access Charge Order.

The Board should stay the Access Charge Order because it violates constitutional standards and New Jersey law rooted in those standards. Under both constitutional and statutory requirements, the Board must set rates for services that it regulates so as to permit Verizon NJ an opportunity to recover the costs it incurs to provide those services, along with a constitutionally adequate return of and on investments needed to provide such services. The Access Charge

Order violates these requirements: it takes away access revenues that were designed to subsidize below-cost retail rates, without rebalancing the retail rates or reducing Verizon NJ's retail service obligations. As a result, Verizon NJ would realize even greater negative returns on services classified as "non-competitive" that remain subject to the Board's rate regulation.

Moreover, the situation in New Jersey is unique in several respects: the retail rates set by the Board remain among the lowest in the nation; Verizon NJ already is losing **[BEGIN VERIZON NJ CONFIDENTIAL]** [redacted] **[END VERIZON NJ CONFIDENTIAL]** of dollars annually on services subject to the jurisdiction of the Board; and Verizon is in the midst of a massive investment to upgrade its network in the state to the benefit of consumers and the state economy generally. Despite all this, and in stark contrast to other states that have joined incumbent local exchange carrier ("ILEC") intrastate access charge reductions with retail rate rebalancing, the Access Charge Order fails entirely to come to grips with the Board's fundamental regulatory obligation. Verizon NJ should not be required to bear the unlawful revenue losses that the Access Charge Order will produce, which would gravely harm Verizon NJ. So too, the public will be harmed, as the revenue reductions would mean that less is available to Verizon NJ to invest in its network and workforce in New Jersey. Accordingly, the Board should stay the Access Charge Order pending judicial review.

STANDARD FOR A STAY

Four factors must be evaluated when deciding whether to stay an administrative agency decision or order: (1) the likelihood of success by the appealing party; (2) whether the appellant will be irreparably harmed by the denial of the stay; (3) the relative hardships to the parties in granting or denying the relief; and (4) whether there is a settled legal right to the relief sought. *Crowe v. De Gioia*, 90 N.J. 126, 132-34 (1982). A stay is clearly warranted under these criteria.

ARGUMENT

Verizon NJ Is Likely to Succeed on Appeal

The Access Charge Order is unlawful because it produces a confiscatory result, in violation of both constitutional and statutory requirements. Both the U.S. and New Jersey Constitutions prohibit the government from taking private property without just compensation. N.J. Const. art. I § I; U.S. CONST. amend. IV, XIV. As applied in the utility context, the courts have long recognized that the Takings Clause requires a regulator to set rates that permit the utility to recover its costs, along with a return of and on their investments commensurate with the risks of the business. *Duquesne Light Co. v. Barasch*, 488 U.S. 299 (1989); *Federal Power Comm'n v. Hope Natural Gas Co.*, 320 U.S. 591 (1944). Rates that fail to meet these criteria are confiscatory, and a utility cannot be compelled to provide service at confiscatory rates. *Bluefield Waterworks & Improvement Co. v. Pub. Serv. Comm'n*, 262 U.S. 679 (1923).

In evaluating whether the rates set by the regulator meet these standards, the regulator may consider only revenues from the services within that regulator's jurisdiction. *Smith v. Ill. Bell Tel. Co.*, 282 U.S. 133, 148-49 (1930). Accordingly, a state regulator, such as the Board, must establish rates that permit a carrier to earn a constitutionally adequate return on its *intra*state services. *See id.*; *Smyth v. Ames*, 169 U.S. 466, 541 (1898).

The Supreme Court has held that only those rates that the regulator controls and can take credit for—*i.e.*, revenue from regulated services classified as "non-competitive" by the Board—may be considered in determining whether the regulator has met its obligation to provide just compensation. The regulator cannot point to returns earned on the sale of competitive services to satisfy its compensation obligation. *Brooks-Scanlon Co. v. Railroad Comm'n*, 251 U.S. 396 (1920). The regulator is not responsible for the amounts earned for competitive services: the regulator cannot influence the revenue or profits for those services, and correspondingly cannot

ensure that those services produce a sufficient return to make up for any shortfall from the services the regulator does control. Instead, the revenues from competitive services reflect the compensation due to the firm for the risks of a competitive business and cannot be treated as "compensation" for below-cost rates set by the regulator. Barr, et al., "The Gild That Is Killing The Lily," 73 Geo. Wash. U. L. Rev. 429. 462-63 (2005).

The same principles are reflected in *N.J.S.A.* 48:2-21(b), which requires the Board to set regulated rates at "just and reasonable" levels. *See also N.J.S.A.* 48:2-21.18(b). "Just and reasonable" is a term of art meaning that the rates must be compensatory, and not confiscatory, as measured under constitutional standards. *In re Industrial Intrastate Sand Rates*, 66 N.J. 12, 23-24 (1974). Accordingly, *N.J.S.A.* 48:2-21(b) has been construed to require the Board to set rates for rate-regulated services that permit a company to maintain its financial integrity, attract capital, and provide a return commensurate with risk. *Jersey Bell Tel. Co. v State, Dep't of Public Utilities*, 162 N.J. Super 60, 73-74 (App. Div. 1978). In addition, *N.J.S.A.* 48:2-21.19 (b) prohibits the Board from regulating competitive services, which the Board would be doing if it were to count revenue from competitive services in setting access charges. In fact, *N.J.S.A.* 48:2-21.18 (b) prohibits a carrier from "us[ing] revenues earned or expenses incurred in conjunction with non-competitive services to subsidize competitive services." The corollary is equally impermissible – the Board cannot set rates for rate-regulated service based on revenues from competitive services over which it has no jurisdiction and which are already price-constrained by competitive market forces.

The Access Charge Order violates these fundamental requirements. It sets rates that do not provide Verizon NJ sufficient revenue to recover its costs and earn a return of and on its investment with respect to rate-regulated services that it is compelled to provide. On the

contrary, Verizon NJ's revenue from all rate-regulated intrastate services is already **[BEGIN VERIZON NJ CONFIDENTIAL]** [redacted] **[END VERIZON NJ CONFIDENTIAL]** *lower* than its costs of providing those services. Vasington/Mazziotti Direct at 30. Indeed, Verizon NJ's 2008 annual report, which was filed with the Board on March 31, 2009, shows net regulated intrastate operating income (for intrastate "competitive" and "non-competitive" services) of **[BEGIN VERIZON NJ CONFIDENTIAL]** [redacted] **[END VERIZON NJ CONFIDENTIAL]** *before* interest expense and taxes (which must also be taken into account). *See* Annual Report of Verizon New Jersey for the year ended December 31, 2008. By slashing the rates for intrastate access, without making any offsetting changes to Verizon NJ's retail rates or service obligations, the Access Charge Order makes this situation substantially worse and ensures that Verizon NJ will earn a negative return both on services classified as "non-competitive" that remain subject to the Board's rate regulation, and on all intrastate services subject to the Board's jurisdiction.

The Board's previously issued ILEC Reclassification Order is wholly insufficient to resolve this defect, and it was not intended to do so. That Order caps Verizon NJ's local rates at levels well below its costs for providing local service. In fact, on an inflation-adjusted basis, the rates authorized by the ILEC Reclassification Order remain *lower* than what Verizon NJ was permitted to charge in 1985. ILEC Reclassification Order at 28. In other words, the ILEC Reclassification Order *partially* remedied the fact that Verizon NJ's local rates had not increased since 1985, but it did *not* authorize Verizon NJ to fully recover its costs for local service through its local service rates – and it did nothing to adjust the Board's historical policy of relying on a contribution from switched access to help make up the shortfall. On the contrary, even if the limited price adjustments permitted under the ILEC Reclassification Order were fully

implemented (and could be sustained in the face of intense competition from cable and wireless voice providers), Verizon-NJ would still lose approximately **[BEGIN VERIZON NJ CONFIDENTIAL]** [redacted] **[END VERIZON NJ CONFIDENTIAL]** dollars a year whether one were to consider all regulated intrastate services or just services classified as non-competitive by the Board. *See* Vasington/Mazziotti Direct at 37; Annual Report of Verizon New Jersey for the year ended December 31, 2008; Vasington/Mazziotti Rebuttal at 27. Thus, the limited rate flexibility provided in the ILEC Reclassification Order was insufficient on its own terms, and certainly does not entitle the Board to reduce intrastate access charges to levels that leave Verizon NJ with revenue from intrastate rate regulated services that is far below its costs of providing those services.

Because the net effect of the Board's rate regulation is to produce revenues that do not even come close to covering Verizon NJ's cost of providing rate regulated services, let alone allow it to earn a return on investments necessary to provide such services, the Access Charge Order is plainly invalid. Although revenues from competitive services may not be considered in determining whether the rates set by the Board are compensatory, such revenues in any case would not be sufficient. Even if revenues from competitive intrastate services were considered, Verizon NJ would still earn a negative return upon implementation of the Access Charge Order, as demonstrated above. *See* Annual Report of Verizon New Jersey for the year ended December 31, 2008. Accordingly, the Access Charge Order is confiscatory and hence invalid under any measure.

The Access Charge Order fails to come to grips with these fundamental flaws. The Board never states that its regulated rates are compensatory. Instead, the Board attempts to avoid the issue by stating that "the question of revenue recovery is not part of this proceeding," and

suggesting that Verizon NJ may be able to seek such recovery in an unspecified "separate proceeding." Access Charge Order at 28. But the Board cannot set rates that fall short of the constitutional minimum, nor can it avoid scrutiny of that issue by suggesting that it might consider offsetting rate changes at a future date.[1] The Board is obligated to ensure that the constitutional minimum of compensation is satisfied when it sets *these rates*. *Hope Natural Gas*, 320 U.S. at 602 (requiring examination of the net effect of the rate order). This is an application of the general principle that when the government takes property, it must make a "reasonable, certain, and adequate provision for obtaining compensation *at the time of the taking*." *Preseault v. ICC*, 494 U.S. 1, 11, 110 S.Ct. 914, 108 L.Ed 2d 1 (1990) (citations omitted) (emphasis added). Because the Board failed to ensure that its rates would be compensatory *before* they go into effect, the Access Charge Order is unlawful.

Strict adherence to these principles is especially necessary in this context. This is not a situation in which rates that are designed to be compensatory nevertheless may turn out not to produce revenues sufficient to meet the constitutional minimum. Instead, the Access Charge Order eschews any effort to determine whether the rates established will be compensatory. In other words, the Access Charge Order fails to apply an essential criterion in determining the proper rate levels. As such, the Order not only violates the substantive requirement that rates not be confiscatory, but also is arbitrary and capricious. *In re Herrmann*, 192 N.J. 19, 28 (2007)

[1] Moreover, the Board's assertion that its "determination" that "revenue recovery would not be determined in this proceeding" was "not challenged by any party" is plain error. Verizon NJ repeatedly objected to the Board's refusal to ensure revenue recovery. *See e.g.* Vasington/Mazziotti Direct at 5 ("[I]t would be counterproductive to further reduce by regulatory fiat the revenues from intrastate access services without simultaneously providing an opportunity for offsetting revenue increases to other rate-regulated services to the extent the competitive market may permit.") *See, also,* Verizon Initial Brief at 2 (italics in original) ("[T]he Board could consider reducing the uniform benchmark *but only if* the Board were at the same time also to eliminate the legacy regulatory burdens that have historically been supported through the implicit subsidies contained in these access charges.")

(administrative agency decision is arbitrary and capricious where agency has failed to consider the relevant factors).

Compounding its failure to allow for a constitutionally adequate return, the Access Charge Order also purports to require Verizon NJ and other ILECs to act as carriers of last resort – that is, to provide service on demand to all – and to do so regardless of cost and without adequate compensation under the Board's regulatory scheme. This carrier of last resort obligation, which is not supported by the sole statutory authority cited by the Board, also violates another bedrock constitutional privilege. *See United States v. Pewee Coal Co.*, 341 U.S. 114, 117-18 (1951) (plurality) ("When a private business is possessed and operated for public use, no reason appears to justify the imposition of losses sustained on the person from whom the property was seized."); *In re Permian Basin Area Rate Cases*, 390 U.S. 747, 770-73 (1968) (discussing utility's right to seek waiver from rate regulation when regulated revenue does not cover out-of-pocket expenditures).

Indeed, the net effect of the Board's regulatory regime is plain. Verizon New Jersey already suffers a negative return both on the services the Board classifies as non-competitive and subject to rate regulation, and also on the broader set of intrastate services subject to the Board's jurisdiction. By dramatically reducing a significant source of contribution to below-cost local retail rates without concurrently implementing any offsetting changes, the Access Charge Order exacerbates this situation. The result is that Verizon NJ is obligated to provide rate regulated services at a loss. As such, the Access Charge Order is invalid under both constitutional and statutory principles.

Verizon NJ Will Suffer Irreparable Harm Without A Stay

A stay is needed to prevent irreparable harm to Verizon NJ. The Access Charge Order requires Verizon NJ to reduce intrastate access charges by February 21. This will have an immediate impact on Verizon NJ's business. Verizon NJ estimates that it will lose **[BEGIN VERIZON NJ CONFIDENTIAL]** [redacted] **[END VERIZON NJ CONFIDENTIAL]** of dollars in access revenue under the order. *See* AT&T/VNJ 2-45(a) marked as Exhibit AT& T -62C. *This* is not a simple financial loss that can be remedied later. The effects of the revenue loss, coming at a time that Verizon NJ is *already* operating its rate regulated intrastate business at a loss, would be particularly acute and would be irremediable. Verizon needs these revenues to continue to invest in New Jersey, operate and maintain the network, and maintain a strong workforce. The reduction in available revenues the Access Charge Order requires will, therefore, have immediate and long-term consequences for the network and Verizon NJ employees. These harms cannot be remedied, even if the Board were to try to correct its order later to allow Verizon NJ to eventually recoup the difference between its existing rates and the unlawful rates set by the Access Charge Order. In addition, the Board has not committed to providing a true-up if the Access Charge Order is invalidated. Even if it did order a true-up, interexchange carriers may not have the financial capacity to repay the amounts owed. Hence, Verizon NJ's ability to recoup its losses is uncertain, and this uncertainty constitutes irreparable injury.

The Balance Of Hardships Favors A Stay

The balance of hardships also favors a stay, which would preserve the *status quo*. On one hand, Verizon NJ's intrastate access charges have been in place for many years, and competition for interexchange services is flourishing in New Jersey. On the other hand, implementing the Access Charge Order would irreparably harm Verizon NJ, its employees, and its customers.

Verizon NJ Has The Right To Request The Relief Sought

Because the Board's order violates state and federal law, and would drastically reduce Verizon NJ's revenues, Verizon NJ has a settled legal right to request a stay of the Board's unlawful order.

CONCLUSION

For the reasons set forth herein, Verizon NJ respectfully requests that the Board stay its enforcement of its order by February 5, 2010.

Respectfully submitted,

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